Summary

Nova Scotia is in better financial shape than it has been in a generation.

Our plan to reduce the provincial debt means more money will be available for health care, education, better roads — for all of our priorities.

By carefully managing the province's finances over the past four years, the provincial government has moved Nova Scotia from spending more than it takes in each year to small surpluses. Not only have the last two provincial budgets been balanced, several other positive actions—steady reduction in net direct debt to GDP ratio, sharp reduction in foreign currency exposure—clearly show that Nova Scotia is on the road to financial recovery and prosperity.

The next step on Nova Scotia's road to financial strength is to stop the slow growth of our provincial debt and then to start paying it off.

The provincial government debt reduction plan consists of three parts. They are:

1. Commit to a yearly, increasing budget reserve fund for debt reduction, starting in fiscal year 2004–05. The reserve and the budgeted surplus must reach $70 million by fiscal year 2007–08.

2. Using a portion of interest earned on investments, create a fund specifically for debt retirement; and

3. Enact legislation that commits extraordinary revenues to the province, as well as money from the sale of provincially owned assets, to the debt retirement fund.

The plan in the following pages provides details on each of these parts and shows how our provincial debt will start going down in a few years.

The same leadership, political will, tough choices and patience that we used to balance our budgets, will be used to reduce our debt.

Nova Scotians can be confident it will happen, just as our balanced budgets happened.

The benefits of lower provincial debt are near and they'll increase with time and success.

Debt management and debt reduction are the next steps toward Nova Scotia's stronger, more prosperous future.

Introduction

This year almost 900 million of Nova Scotians' tax dollars will be needed just to pay interest on the province's $11.7 billion debt. That money will never pay a Nova Scotian doctor, buy a book for a student, pave an inch of road or help a family down on its luck. That's the bad news.

The good news is that Nova Scotia is now, for the first time in a generation, in a position to do something about it. We are now in position to put in place a responsible, attainable plan to stop growing, and then start reducing, the provincial debt.

In the longer term, lower debt will reduce our annual interest charges. But the benefit of debt reduction will be apparent much sooner and the impact will be magnified as the financial world sees our fiscal position continue to improve. Nova Scotia will become a better credit risk. Our rating will improve and the cost of borrowed money will decline. We will be off the downward debt spiral, and on the upward spiral of growing financial strength.

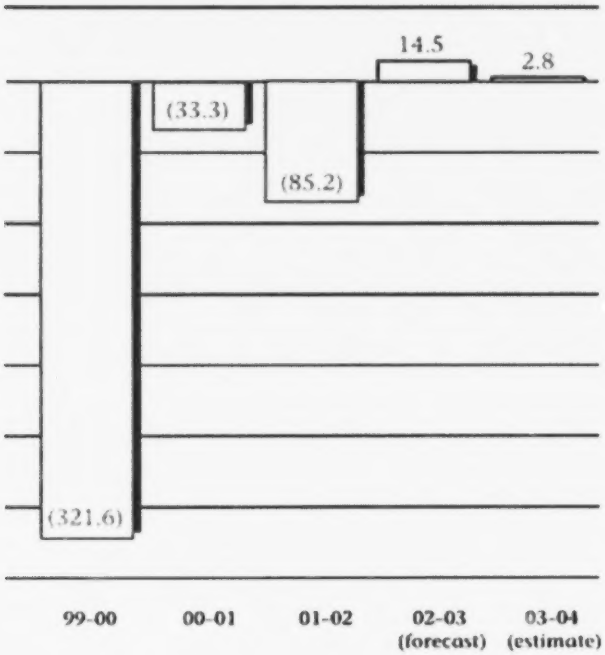
Why Are We in a Position to Talk about Debt Reduction?

As a province, we are now in this more favourable position because of four recent and important actions on the part of government. One: In 1999, government consolidated the books. The province's financial statements now report on all aspects of government. There are no hidden or "off-book" expenditures. Two: Also in 1999, and in conjunction with consolidation, government adopted generally accepted accounting principles (GAAP). Consistent with GAAP, we started amortizing the cost of tangible capital assets. Accounting is continually evolving. As accounting changes come forward, we are committed to instituting recommended changes. Three: Government has reduced its business risk. It has sold Nova Scotia Resources Limited (NSRL), closed Sysco and dramatically reduced its foreign currency exposure. These decisions have had a significant impact on the operations of the province. And, four: In 2002–03, and again this year, 2003–04, the government balanced its budget.

It is by design, and not by accident, that these initiatives resulted in our ability to begin the plan for debt reduction. For the first time in living memory, the province could calculate when the debt would stop growing. In 1999 the trend was very different. Just four years ago the debt in Nova Scotia was never going to stop growing. Generations of Nova Scotians, yet unborn, were destined to a future that, like our immediate past, sentenced them to ever-higher debt and the interest payments that go with that debt.

Nova Scotia Surplus (Deficit) 1999–00 to 2003–04

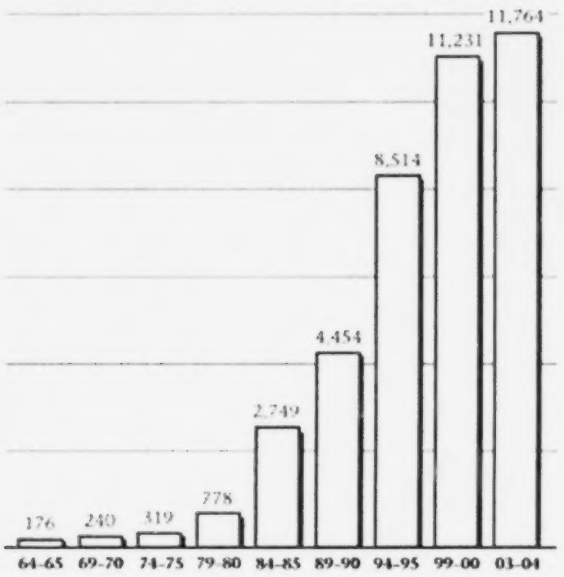
(before unusual items, in $ millions)



Two balanced budgets, with more to follow, broke a 40-year trend of deficit financing in Nova Scotia. Past deficits are largely responsible for the province's $11.7 billion debt. Indeed, the purchase of tangible capital assets—roads, schools and other public infrastructure—accounts for just about $3 billion of the debt. Deficits of government and losses of Sysco and NSRL are to blame for the remainder.

Historic Net Direct Debt Growth 1964–65 to 2003–04

(in $ millions)



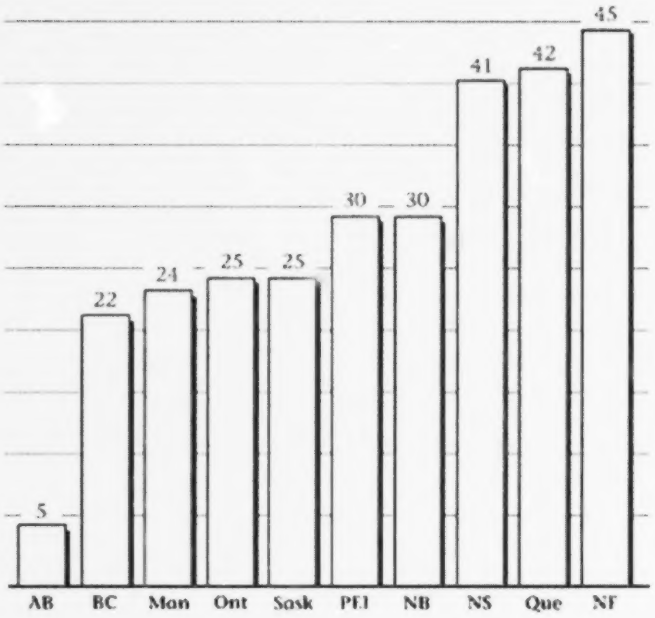
Source: Province of Nova Scotia Public Accounts
Provincial NDD based on 2003-04 Estimates presented in budget.

With balanced budgets, it should be noted, the only additional debt in the last two years came from the purchase of capital assets. In other words, Nova Scotia now has something to show for the money it borrows—roads and schools.

While we have come a long way financially in a relatively short time, we still face challenges. Our fiscal position, while improved, is still weak compared to other provinces. Nova Scotia carries one of the highest per capita debt ratios in the country. Our net direct debt to Gross Domestic Product (GDP) ratio, while also improving, is also among the worst in the country. Net direct debt to GDP compares what the province owes with what it produces, thereby measuring the province's ability to manage its debt. It is similar to considering a family's situation—the more the family members earn, the greater its capacity to meet necessary financial obligations.

Provincial Net Direct Debt/GDP Ratios Based on 2003–04 Estimates

(per cent)



Source: Fiscal Pulse, Scotiabank Global Economic Research
(all numbers have been rounded to the nearest %)

In 2002, the province set the foundation for its debt reduction plan. A Balanced Approach to Surplus and Debt Management spoke about the need for balanced budgets and the impact of surpluses on containing the debt.

Two balanced budgets, a $250 million annual capital spending limit, have the province's public spending well under control. Capital spending at this level will allow for a prudent investment in much-needed capital infrastructure. Investing in capital infrastructure will have a positive impact on the province. Steady economic growth, lower taxes and an increasingly competitive tax environment, plus a declining dependence on federal transfers creates a more self-sufficient province.

All of this has positioned the province well. It can now move beyond management of the debt to take the next step—a step that will see debt plateau and actually begin its decline in 2007–08.

The debt reduction plan calls for commitment and discipline, but its goals are attainable. After all, with the same kind of commitment and discipline, the province's annual operating deficit, which stood at $321 million on March 31, 2000, was eliminated last year.

Like the successful effort to balance the budget, the debt reduction plan is also based

on a graduated approach. It can be accomplished without abandoning the essential capital investment program of the province, without harming our investments in health care, education or in other public services. But it will require determination, hard choices, setting priorities and a strong commitment from the government and the people of Nova Scotia.

The Debt Reduction Plan

The province is ready now to take the next, important steps toward reducing that debt. In the spring of 2004, the province will give its debt reduction plan the force of law as part of the Financial Measures Act. This action is consistent with the successful approach to balancing the budget, also enshrined in legislation enacted in 2000.

The debt reduction plan consists of three distinct, but related initiatives.

First, the province will generate budget surpluses large enough to offset capital spending less amortization. That will be accomplished by 2007–08, with the equivalent of a budgetary surplus of about $70 million.

Like the balancing of the budget, this objective requires a graduated approach to ensure success. In each of the next three fiscal years—2004–05; 2005–06; 2006–07—the province will establish a separate budgetary expenditure item for debt reduction. The debt reduction reserve and budgeted surplus will increase each successive fiscal year, reaching $70 million by 2007–08. The province will continue to invest $250 million a year in capital infrastructure.

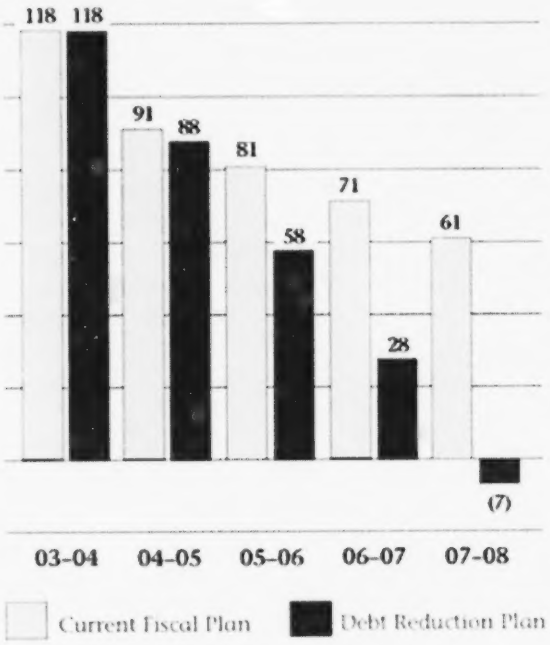
The legislation will prescribe that a separate budgetary item be allocated for debt reduction. This will help make the targets real, demonstrating our commitment to debt reduction. The legislature will be asked to approve the debt reduction allocation and the government will only be able to reallocate funds for purposes outlined in the legislation.

The second and third measures of the plan involve contributions to a new debt retirement fund, also established by legislation.

The debt retirement fund will be created by an annual deposit of $6 million, beginning in 2004–05. These funds will be directed from interest earnings accrued on investments currently used to offset debt servicing costs. As legislated, these investments will be left to accumulate compound interest. At strategic intervals, beginning in 2007–08, the province will be able to make payments directly on the principal of the debt.

Surplus and Capital Spending Impact on Net Direct Debt 2003–04 to 2007–08

(in $ millions)



These interest revenues come at a price—debt servicing costs will increase by about $6 million per year, at a minimum, imposing additional discipline on the budget process. However, the compound interest on the annual deposits will, in just four years, exceed the $6 million in annual costs.

The final measure of the plan will dictate that extraordinary revenue accruing to the province will also flow to the debt retirement fund, as will gains from the sale of any and all Crown assets. Applying the gains from the sale of Crown assets is consistent with current practice. Indeed, proceeds from the sale of Nova Scotia Resources Limited have already offset some of the provincial debt.

All extraordinary revenue that falls into this category will be clearly defined in the legislation. The characteristics of the definition will include that extraordinary revenues are not part of the normal course of business, that they are not expected to occur on a regular basis and they cannot be influenced by decisions of government. It will include, for example, the offshore Crown share payments from the federal government owing to the province.

The legislation will not limit revenue sources to be used for debt retirement, but will prescribe that certain extraordinary revenues be used only for debt retirement. Government will be able to voluntarily increase revenues destined for the fund, but

will be unable to divert certain defined revenues away from debt retirement.

In short, the debt retirement fund can grow in a number of ways. Extraordinary revenues; voluntary revenues; accumulated interest; additional interest revenue deposits or the gains on sale of assets. All of this will provide the additional push that will complement the financial objectives of the annual, budgeted efforts of debt reduction.

Light at the End of the Tunnel

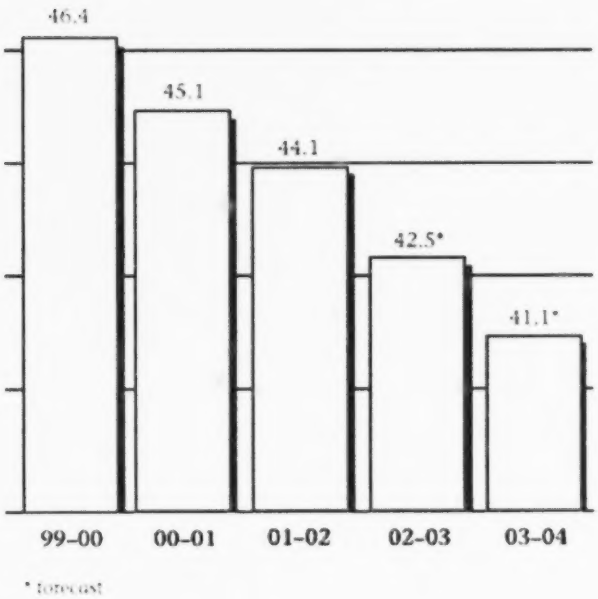
It has taken decades to accumulate this debt. It will not be eliminated in the short term. But we have already made a great deal of progress.

The province has consolidated government accounts so Nova Scotians can see the true measure of the problem. It put the brakes on government spending growth and passed laws that would mean a balanced budget by 2002–03. In fact, it did more than promise.

Sysco was closed. NSRL was sold and gains from the sale used to offset the debt. Government services were reviewed and reorganized. Foreign currency exposure was reduced from 51 per cent in 1998–99 to 19.7 per cent by the end of 2002–03, making the province's debt servicing costs less vulnerable to the volatility of fluctuating currency markets.

Net Direct Debt to Gross Domestic Product Ratio 1999–00 to 2003–04

(per cent)



We have done all this while investing tens of millions of dollars in the areas that are of highest priority to Nova Scotians. The province has put books and computers in classrooms. It developed plans that help prioritize and pay for critical health care. Government has put in place strategies that will help grow the economy, that will lower taxes and keep Nova Scotia a competitive place in which to do business and a secure, positive place in which to live.

Two successive balanced budgets and good economic planning have put Nova Scotia on the road to prosperity.

Just four years ago, the province's net direct debt to GDP ratio stood at 46 per cent. It is now 41 per cent. Nova Scotia is registering record-breaking employment rates—29,900 new jobs have been created since July of 1999, 90 per cent of them full-time positions.

With hard work and determination, we have stopped borrowing money to meet our operating costs. The province has lowered taxes while continuing to advance plans that help invest in high quality health care, good education, safe roads and a competitive, vigorous business climate.

The plan for a more prosperous Nova Scotia continues to work. The next step is to

reduce the debt, continuing to build a Nova Scotia that makes, and pays, its own way in the world.

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